FOREIGN SERVICE OF THE UNITED STATES OF AMERICA

EUR INDEX

81
25

EXCISE

SECURITY : CONFIDENTIAL PRIORITY: AIR POUCH

TO : Department of State July 28, 1950

FROM : BRUSSELS 72

REF : 755.00/7-2850

XR 855.00

SUBJECT : Interview with Governor Frere of the Belgian National Bank, Tuesday, July 25, 1950

For Dept use only
RECD AUG 8

ACTION EUR

INFO FR DCR UNA OLI USUN E ECA TR

PASS TREASURY AND ECA.

This report of a conversation with Governor Frere is lengthy. However, we feel that the Governor was unusually frank in this interview with Mr. Judd Polk, U. S. Treasury Attache, and Mr. William B. Dale, Assistant U. S. Treasury Attache, and that his remarks have such special interest in view of the disquieting situation in Belgium that they warrant detailed recording.

The Governor dealt with:

(1) The general political situation, about which he expressed deep anxiety. [redacted]

(2) Public finances, which he regards as at a low point in Belgian postwar history and as a menace to the degree of stability which has been attained at great sacrifice.

(3) The military responsibilities of Belgium, to which he assigns first priority. [redacted]

(4) The role of Belgium in the European economy (EPU). He expressed (surprisingly) satisfaction and was hopeful of the prospects of EPU.

(5) Benelux. Although he returned from an Italian vacation for the Ostend conferences, he considers very little will be accomplished there. [redacted]

He also provided exact information on the Dutch debt to Belgium.

DEPARTMENT OF STATE A/CDC/MR
REVIEWED BY J. L. SMITH DATE NOV 2 2 1982
RDS☐or XDS☐EXT. DATE
TS AUTH. REASON(S) 1.3(a)(4)
ENDORSE EXISTING MARKINGS ☐
DECLASSIFIED☐ RELEASABLE☐
RELEASE DENIED☐ IN PART
EXCEPTIONS

WRD
WBDale/eeh
JP 501.6
AUG 2 1950

ACTION COPY - DEPARTMENT OF STATE

The action office must return this permanent record copy to DC/R [illegible] with an endorsement of action taken.

B-1 mls

B-1

755.00/7-2850

B-1
RM
RML
GF
RMW
mc

FILED

HH

I. The Political Situation in Belgium

Frere stated he had come back from a vacation in Italy, to which he will return next week, in order to attend the Benelux Conference at Ostend during the coming weekend. He also wants to see some of the Belgian Ministers, particularly the Finance Minister, to discuss some problems which he considers serious.

Throughout the interview, during which he appeared tired and anxious, Frere emphasized his great concern over the political situation in Belgium. Since the formation of the Eyskens Government in August 1949, politicians have been so intensely occupied with the Royal Question, he said, that they have had little time for considering other problems.

The Governments for the past year have been both short-term and special-purpose, and this has led to a large degree of irresponsibility, particularly in fundamental economic and financial policies. With the return of the King, all parties have taken such extreme positions that political cooperation among them on any question is almost impossible. At least it is out of the question for this Government to act decisively on the important questions facing the country.

Before the Royal crisis, Frere said, the Ministers listened with some interest and respect when he ventured a suggestion on financial policy. Now, however, he finds it impossible to secure even a hearing.

[redacted] B-1

The Socialist strikes, Frere expects, will undoubtedly include wage demands which the Christian Socialist unions will have to duplicate and which could seriously upset the country's economic equilibrium.

[redacted] B-1

II. The Budget and Treasury Situation

Frere is very worried over the position of the Treasury. On one day last week the Treasury had only 200 million francs of credit remaining available to it at the National Bank. At present the situation is somewhat improved, and the Treasury has about one billion francs of credit, but Frere regards the improvement as transitory. He expects a serious crisis for the Treasury this Fall.

Asked the reason for the adverse Treasury situation, Frere stated that there are three chief reasons, andy many subsidiary ones. Basically, he feels, it results from the irresponsibility of recent Governments, which have failed to face realistically the problem of keeping their obligations within the limits of their financial facilities. Beyond this, the three chief reasons for the crisis are the large, and partially needless, public works program, the Government's program of promoting housing, and the expenditures for unemployment compensation.

The greatly increased public works program was introduced by the Eyskens Government to help solve the unemployment problem. But, since Frere believes the problem of unemployment is much smaller than is commonly supposed ("Have you ever seen an unemployed?"), he considers the public works program as having little bearing. He welcomes the construction of new roads and port facilities, particularly at the present moment because of their military significance, but he believes much of the public works program could be postponed. Few of the projects are objectionable in themselves, but, for Frere, the policy must be judged in the light of the utter failure of the Government to assign priorities in its program, or in fact to have a program at all. It wants to have everything at once.

[redacted] B-1

The public works program, in this light, was inspired by political considerations, not by a real or coherent policy on the unemployment problem itself.

The public housing program results from the de Taeye law, passed several years ago. It has been applied, however, only for the past year and represents another of the programs of the Eyskens Government. The law provides that persons building new homes will receive premiums from the Government and can borrow a substantial part of the remaining cost from the Caisse d'Epargne. Frere does not know how much the premiums have cost the Treasury, but it seems likely that they have been around 1.5 billion francs in the past year. A real difficulty, however, has been created for the Caisse d'Epargne. When the de Taeye law was passed, it was expected that it would oblige the Caisse d'Epargne to loan about 5 billion francs over a five-year period. But the demand for housing has been so heavy that the Caisse d'Epargne has been forced to loan 3 billion francs in the first year on this account, and the demand shows no signs of abating.

Normally, the Caisse d'Epargne forms a reservoir for the Government to draw on when it needs funds. The fact that the Caisse d'Epargne has usually had reserves which it could invest in Treasury bills has given the Government a second source of temporary financing after the National Bank. Now, however, the housing loans have taken nearly all the reserves of the Caisse d'Epargne at a time when many of the Government's financial commitments are coming due and it is forced to look for sources of financing. Several other factors have combined to render the situation of the Caisse d'Epargne particularly

difficult at the present moment. It is normal for deposits at the Caisse d'Epargne to decline somewhat in July and August, because savers draw money to finance vacations. Usually the Caisse has sufficient reserves to take care of this withdrawal and also to help the Treasury in the summer months when tax receipts are likely to be lower than usual. This summer, the housing loans have made this impossible.

In fact, the Caisse d'Epargne has been forced to sell some of its Government securities on the open market and to rediscount more of them at the National Bank. Since credit given by the National Bank to such parastatal organizations is included under the ceiling of 10 billion francs on the Bank's advances to the Government, the Government's line of credit at the Bank has been correspondingly reduced. The Caisse d'Epargne has been a borrower rather than a lender to the Government.

In addition, the prices of Government securities have been falling, and the Bank has had to support them through the Fond des Rentes, a parastatal organization created for this purpose. This, too, has used some of the Government's line of credit at the Bank. The Caisse d'Epargne's Government security sales have undoubtedly contributed to the fall in their price, although the international political situation has been the chief factor. In this connection, Frere said that the amount of Belgian franc bank notes sent to the National Bank from abroad has more than doubled since war broke out in Korea. He takes this as evidence of capital flight from Belgium in the last month.

Lastly, the fall in Government security prices occurred at a time when the National Railways were trying to float a loan for one billion francs. Frere said that this loan has not been a success, and, after three weeks, a large portion of it is still in the hands of banks. On the basis of this performance, he regards the Government's internal borrowing power as nil at the moment.

The Government expenditures for unemployment compensation and sickness insurance (to cover only the deficits of the social security system in these fields) were almost 6 billion francs in 1949, as against an original estimate of less than 2 billion francs. The extent to which this resulted from a real increase in unemployment, as against people taking advantage of the liberal provisions of the laws and regulations, is not clear, but Frere definitely favors the latter explanation. In any case, these large expenditures have been an important factor leading to the present shortage of Government funds.

Frere mentioned several other factors which contributed to the present situation. One was the reduction in direct taxes which Finance Minister Liebaert introduced last fall. The measure did not cost much revenue last year, Frere said, but it set an improper trend. It resulted from the Liberal campaign slogan that they would reduce direct taxation by 25 percent. Frere believes Liebaert introduced the measure immediately upon becoming Finance Minister without making any adequate investigation of its probable effect on

the financial position of the Government. Liebaert is now gone, but the legacy of his irresponsibility remains. The tax reduction cost the Government about 300 million francs of revenue in 1949, and will cost over one billion francs for 1950. This in itself is not decisive, but that it happened at a time when the Government was undertaking large new financial commitments was very important. The trend which has been set will make it extremely difficult to raise taxes, as they must be if the Government's financial problem is to be solved.

In sum, Frere believes any Belgian Government which is to solve the financial problem must develop a firm and reasoned program by reforming social security legislation, and assigning much lower priorities to housing and public works programs. He does not expect such a Government in the near future. A year ago, the National Bank's advances to the Government stood at 5 billion francs. Today, they are about 9 billion francs. The crisis which Frere expects this Fall will prompt the Government to ask Frere to raise the present ceiling of 10 billion francs on these advances. He expects to be forced to raise the ceiling, but he intends to call attention to the Government's financial irresponsibility by taking a firm public position in the matter.

He expects the same thing to happen as regards the profits of about 4 billion francs resulting from the revaluation of the National Bank's gold. Frere has no objection whatever to these profits being taken by the Government. Four billion francs of profits for the 200 million francs of National Bank shares in private hands would obviously be out of the question. He does, however, seriously object to their being commingled with other Treasury funds and being used to cover budget deficits. His position, which he has made quite clear, is that the profits should be used entirely to repay part of the Government's consolidated debt to the Bank (now around 34 billion francs). Frere feels that he has won a considerable concession in this question, since the bill on the profits which is now before Parliament provides that the profits will be turned over to the Government, but will be kept in a special account at the National Bank. The use to be made of the funds will be subject to legislative decision later, probably not before Fall. Frere feels this solution will permit the public to focus its attention on the specific use to be made of the funds, and will thus constitute an important check on the Government.

III. The Problem of Building Military Preparedness

Frere indicated that he believes the matter of increasing military preparedness should be given the highest priority in the present international situation. He deprecated the political situation in Belgium which is at present preventing adequate concentration on the larger fundamental issues, such as this one which is now facing the country. He does not look for any Belgian Government to be in a position of exercising effective leadership and taking firm decisions in the defense field in the near future.

We pressed Frere fairly hard on the question of what the financial capacity of Belgium would permit in the way of increasing military production. He indicated his firm belief that the overall budgetary expenditures of the Government should not be increased, even in a period of increasing military expenditures. He also would oppose increasing the ceiling on National Bank advances to the present Government. His position, therefore, boils down to advocating a shift in budgetary expenditures from other fields into the military field. Asked to give an estimate of the practical possibilities of such shifts, he said he did not have the budgetary figures sufficiently well in mind to give any sound analysis, but he believes that perhaps 3 or 4 billion francs could be found within the budget for expenditure on military production. It seems likely that he would advocate shifts chiefly from certain types of public works and from unemployment compensation payments.

IV. European Payments Union

We asked Frere his opinion of EPU, and he seemed to feel he was making a real concession when he said that it may not turn out to be as bad as he had expected. The character of EPU, he indicated, will be determined by how the agreement is interpreted in practice, which in turn is a problem of what kind of powers the management will have and how it will exercise those powers.

In speaking about EPU, Frere indicated that he had reached an agreement with the Belgian Government that the National Bank would finance no more than $120 million of the total credit which Belgium may be called upon to extend to the organization. Although no action has been taken on this agreement [illegible]ly, Frere considers it firm. If Belgium should use its entire quota $360 million in the first year (and assuming that her initial debit position is $55 million), the credit which Belgium would have to extend to EPU would be $188.5 million. If the quota is used in two years and if the Belgians receive a further $25 million of conditional aid in 1951/52, the total credit extended by Belgium in the two years would be $176 million, which under the National Bank/Government understanding would be put up 2/3 ($120 million) by the Bank and 1/3 by the Government.

Frere wants to implement this agreement by dividing the credit to be extended to EPU at each settlement in this ratio of two to one. He is also thinking of suggesting that the Government could meet its share of the credit by turning over to the Bank 3 billion francs of the profits on the revaluation of the National Bank's gold. The latter technique, however, might confuse his position that the gold profits should be used for retirement of the Government's long-term debt. He agrees that there would be no important financial difference between using the revaluation profits for reducing the Government's consolidated debt to the Bank and in using them to cover the Government's credit obligations toward EPU, but he wants to keep his position on the use of the revaluation profits perfectly clear.

V. Benelux

As is mentioned above, Frere returned from his vacation in Italy specifically to be present at the Benelux Conference at Ostend July 29 through 31. He said the Belgian delegation will be large and will be headed by five ministers -- the Prime Minister, the Foreign Minister, the Finance Minister, the Minister of Economic Affairs, and the Minister of Public Works. Both Frere and Ansiaux will be there.

Frere is of the opinion that little of real importance will be accomplished at Ostend. He believes that the agricultural problem will be the most important matter for the conference, and that the problem of the Dutch bilateral debt to Belgium will not be a particularly thorny one at this meeting. [redacted] B-1

APPENDIX

Bilateral Debt of The Netherlands to Belgium

Frere explained that the bilateral debt of The Netherlands to Belgium to be amortized through the EPU mechanism will be either $68.8 million (B.F. 3.44 billion) or about $63 million (B.F. 3.15 billion). It will be the latter amount if a second category compensation, proposed by the Agent in connection with the June IEPA operations, and accepted by Belgium, is carried out. Neither of these figures include the $38 million loaned to The Netherlands by Belgium under the IEPA for 1949/50, since this credit is a long-term obligation and no repayments will be made in the next two years.

Specifically, the bilateral debt as of June 30, 1950, breaks down as follows:

1.	Current payments agreement account, after adjustment for drawing rights and Belgian credits used in June operations	$36.8 million	(B.F. 1.84 billion)
2.	Accounts already consolidated, with agreed provision for complete repayment by the end of 1951	32.0 "	(B.F. 1.60 billion)
	Total	$68.8 "	(B.F. 3.44 billion)

The second category compensation mentioned above, which apparently involves about $6 million (B.F. 3.00 million) on each leg, would, if carried through, reduce the current payments agreement account to about $31 million (B.F. 1.55 billion) and reduce the total bilateral debt to about $63 million (B.F. 3.15 billion).

At the end of June, the current payments account stood at about $48 million (B.F. 2.4 billion) in favor of Belgium. This will be reduced by $11.2 million (B.F. 560 million) by virtue of drawing rights and long-term Belgian credits which will be utilized by The Netherlands in the June operations. This will bring the account at the end of June to $36.8 million (B. F. 1.84 billion). The proposed second category compensation would further reduce it to about $31 million (B.F. 1.55 billion). Developments in this account since the end of June show a Belgian surplus with The Netherlands of about $12 million (B.F. 600 million) for the period July 1-24. This surplus will, of course, be handled as a normal current operation in EPU.

The ceiling (or "swing" margin) on the current payments account with The Netherlands is $28 million (B.F. 1.4 billion). The payments agreement with The Netherlands provides that any guilders held by the Belgian National Bank beyond this amount at month's end will be repurchased by The Netherlands with gold in order to bring the account down within the ceiling. This obligation was, of course, partially abrogated by the IEPA, which provided that any such gold payments due would be postponed until after the IEPA operations in respect of the month in question were completed. This, in effect, substituted the use of drawing rights where available for supra-ceiling gold payments by debtors.

However, in June 1950, The Netherlands ran a deficit of roughly $20 million with Belgium and had only $11.2 million of drawing rights and long-term Belgian credits to cover it. The result has been to push The Netherlands definitively beyond the bilateral credit ceiling, with no outside means available to cover the excess. After the June operations are completed, The Netherlands will owe Belgium either $36.8 million or about $31 million on the current payments agreement account, as compared with the ceiling of $28 million. The excess cannot, technically, be covered through EPU, since it did not result from payments made after July 1. If the bilateral payments agreement were strictly applied, The Netherlands would be obliged to pay either $3 million or $8.8 million to Belgium in gold, and the bilateral debt to be amortized through EPU would be reduced to $60 million (B.F. 3.0 billion).

Frere advocates the latter solution. However, the Benelux Pre-Union Agreement of 1949 contained a clause providing that in case a gold payment became due under the bilateral payments agreement, the two parties would consult as to the action to be taken. The implication of the clause is clearly that a way will be found to obviate, or at least postpone, gold payments by The Netherlands. At the time of the Pre-Union Agreement, Frere wrote a strong letter to the Finance Minister indicating that if the effect of the clause was to negate the credit ceiling in the bilateral agreement, he was opposed to it. He further stated that any additional credit given to The Netherlands would have to be financed by the Government, since the National Bank was not prepared to do so. Frere now feels in a strong position to insist that the National Bank not finance the credit which would be given to The Netherlands if the Belgian Government refused to require a gold payment of the supra-ceiling amount. From Frere's point of view, it is immaterial whether the problem is solved by demanding a gold payment from The Netherlands or by the

Belgian Government paying the amount involved to the National Bank in Belgian francs, thus assuming the creditor position toward The Netherlands. The latter solution, however, would precipitate the Belgian Treasury crisis which is feared. Practically speaking, therefore, it seems likely that this supra-ceiling amount will be consolidated with the rest of the debt.

There are two consolidated payments accounts with The Netherlands, one of $22 million (B.F. 1.1 billion) and the other of $10 million (B.F. 500 million). These represent payments credits extended to The Netherlands in the early post-liberation period, and have been consolidated for several years. Regular repayments have been made on the larger account, reducing it from 2.5 billion francs upon consolidation to the present level of 1.1 billion francs. These payments have been handled as current payments and have, during the past two years, been covered by Dutch utilization of drawing rights. Under the present amortization schedule, the total amount of $32 million (B.F. 1.6 billion) will be fully repaid by the end of 1951. Payments of about $20 million (B.F. 1 billion) will be made in fiscal 1950/51 and the remainder, $12 million (B.F. 600 million), will be paid in the last half of calendar 1951. There is, however, a distinct possibility that these consolidated accounts will be renegotiated and included in a general settlement of the entire bilateral Dutch debt to Belgium.

Frere mentioned that some improper aspects of the IEPA were demonstrated by what had happened to the Belgian position with other ERP countries since the end of June. The Belgian assets on France, Portugal, Austria, Denmark, and the United Kingdom have decreased since the end of June, although they increased in June and before. Frere took this as evidence that these countries rushed payments to Belgium during June to get them covered by available drawing rights. This type of action, he believes, skews the natural competitive development of trade patterns and was a major shortcoming of the old payments arrangements. Frere believes the EPU mechanism will correct this flaw.

Robert Murphy

ROBERT MURPHY

Copy to Paris

" " The Hague